

Competitive Market Initiatives

Mass. Department of Telecommunications and Energy

Follow-up Comments of Mirant New England

June 13, 2001

Summary

Mirant New England offers the following comments and recommendations herein:

- Retail competition must be effective, and retail customers must see realistic prices indicative of the full cost of serving retail load.
- The Department and the distribution companies should consider increases to the Standard Offer retail rates to approach the full cost of serving retail load.
- Pilot programs being initiated by the distribution companies should be encouraged and approved by the Department.
- The Department should expeditiously explore the appropriate levels of information the distribution companies should be required to provide to suppliers, as it is critical that appropriate customer load information be provided to competitive suppliers.
- ISO-New England ("ISO") must be held accountable for efficient and impartial administration of the electricity markets.
- The recently announced joint market study being performed by ISO and the Massachusetts Attorney General's office should be expanded to address the complete market and not narrowly focus on one sector.
- ISO-New England governance should be fixed, through an independent, knowledgeable governing board, and by NEPOOL transferring its S.205 rights to ISO-NE.
- The Department and ISO should institute effective demand response programs.
- Massachusetts consumers, and those in New England in general, will benefit from a seamless regional market, and the Department should support a single Regional Transmission Organization for northeast North America.

Discussion

Mirant New England ("Mirant"), an affiliate of Mirant Corporation, is pleased to provide these comments, and intends them to supplement our verbal testimony given at the hearing sponsored by the Massachusetts Department of Telecommunications and Energy ("the Department") on May 31, 2001, and to offer our opinion on the points we heard from various industry representatives and interested parties at same hearing. The hearing was initiated by the Department as a forum to solicit discussion on the state of the competitive electricity markets in Massachusetts and for parties to learn of the initiatives that are currently under way to address issues identified with the current structure. We applaud the Department for sponsoring this event and believe it was effective in raising many parties' level of awareness of the state of the competitive markets, the barriers that are prohibiting the markets from being effective, the need to find solutions which will make the marketing and acquisition of customers more efficient for retail suppliers and the need to find solutions that will allow customers choice in the marketplace.

Mirant Corporation is engaged in the generation and marketing of wholesale electricity and the provision of risk management services in an integrated business model. Although Mirant Corporation is not engaged in retail sales at this time, we believe that the success of retail

electricity markets is inextricably linked to the success of wholesale electricity markets. Liquid and robust retail and wholesale markets send competitive price signals to consumers and can produce in the long run the reliability, customer choice and cost saving benefits of a deregulated marketplace.

In general, Mirant agrees with most of the comments that were made by the four distribution companies on the panel, as well as several of the competitive suppliers. In particular, Mirant supports the following:

1. The Department's recent rulings have appropriately allowed increases to the retail Default Service rates of the distribution companies which more closely and appropriately approximate the true costs of supplying retail customers. In order for retail competition to be effective, retail customers must see realistic prices that are indicative of the full cost of serving retail load, and the recent Default Service rate increases will help effectuate that price signal.
2. The Department and the distribution companies should also consider increases to the Standard Offer retail rates to approach the full cost of serving retail load, similar to the Default Service rates discussed above and in the manner that Western Massachusetts Electric has done, to the extent that there is head-room under each distribution company's 15% rate reduction requirement. Since the majority of customers in Massachusetts still rely on Standard Offer service, the sooner the Standard Offer rates approximate the true cost of retail supply, the sooner competitive suppliers will be able to provide retail offerings that would allow customer migration to competitive supply. Any such changes must recognize and not disrupt, of course, the existing long-term supply agreements that many distribution companies have with their wholesale suppliers for Standard Offer Service.
3. The pilot programs being initiated by the distribution companies as discussed at the May 31 hearing should be encouraged and approved by the Department as learning tools to help understand the barriers which have caused retail competition not to live up to expectations. The programs mentioned at the hearing were being designed to bring more efficiency and ease of entry to the retail markets, including the need to make the flow of information to suppliers more meaningful.
4. In light of the discussion in bullet 3 above about the proper level of customer information, the Department should consider initiating an expedited docket to explore the appropriate levels of information the distribution companies should be required to provide to suppliers. One of the common themes on May 31 was the frustration expressed by suppliers at the inability to obtain customer information that would enable them to price, package and make offerings to various customers and classes of customers. Although privacy of information laws need to be respected, it is critical that appropriate customer load information be provided to competitive suppliers. The general theme from many suppliers was that marketing and acquisition costs in Massachusetts are too high considering the slim margins of full retail competition. Process, procedures and flow of information must be improved in order to lower acquisition costs.

Because the wholesale and retail electricity markets are inextricably linked, Mirant would like to offer the following general comments about the state of the New England wholesale electricity markets:

1. We are concerned that ISO-New England (“ISO”) is not being held accountable for their responsibilities to administer the electricity markets efficiently and in an impartial manner. The scope of the recently-announced joint market study being performed by ISO and the Massachusetts Attorney General’s office, as posted on the ISO website, is limited to “an empirical analysis of the scope and severity of market power in the energy market,” and thus appears to be focused solely on generator bidding behavior, rather than on the entire market. Other areas that a comprehensive study should examine include the behaviors and actions of other market participants such as load serving entities, distribution companies, transmission companies, suppliers and the operation of the bulk power system by ISO itself. NEPOOL Participants are frustrated by the amount of uplift present in the wholesale energy market (which results in a masking of the actual spot price for energy) due to the ISO’s interpretation and implementation of the market rules and the operation of the bulk power system. The prime cause of this energy uplift is the over-commitment of generating resources by ISO. The true costs of wholesale spot energy is not visible to the market because the out-of-merit generation associated with over-commitment is paid through uplift. Therefore, the signals being sent to the market are flawed. Rather than looking at a specific aspect of the wholesale marketplace, ISO should look at the functioning of the marketplace as a whole. Accordingly, we urge the Department to call for such a full market study to better understand the changes in market structures as well as Participant and ISO behaviors that need to be implemented in order to make the markets more efficient. Having correct market signals that are transparent will help the transition towards retail competition. We applaud the ISO’s move towards the Standard Market Design, but believe that changes to the current structure, which will still be in place for well over a year, need to be addressed in order to produce market efficiency and price transparency.
2. The current NEPOOL governance structure is inefficient and ineffective. We believe that a truly independent, knowledgeable markets board needs to be put into place to develop market rules that are consistent with well functioning markets. Ultimately, such a body needs to extend beyond New England and be regional in nature in keeping with the move to a single Northeast RTO. In the interim, and subject to agreement on the processes for ISO and/or Participants to propose market rule changes and for Participant input, Mirant supports transferring NEPOOL’s authority to make S.205 filings under the Federal Power Act to the ISO.
3. An effective demand response program is crucial to the success of the wholesale and retail markets. In that regard, the Department should work closely with ISO to develop effective programs as soon as possible.
4. The New England wholesale marketplace is too small. The FERC, in Order 2000, addressed the market scope issue, which has been interpreted to require marketplaces of roughly 100,000 MW peak demand (NEPOOL’s peak is roughly 23,000 MW). The three northeast ISOs have recognized the need for a larger market in their discussions pursuant to a Memorandum of Understanding to address “seams” issues between the three regions. It is imperative that “seams” issues that currently prevent the movement of low-cost electricity and capacity from one region to another be eliminated. The current MOU process has been ineffective and Mirant encourages the Department to address this

issue by urging the ISO to work toward a fully combined marketplace in the Northeast, not simply three markets with smaller “seams”. ISO’s adoption of a Standard Market Design is a good first step but it does not adequately address seams issues between New York and New England.

We appreciate the opportunity to provide these comments, and are looking forward to participating in further deliberations, hearings or informal sessions on these matters.